No. 84-51

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1984

FLAV-O-RICH, INC.,

*Petitioner,*

v.

NORTH CAROLINA MILK COMMISSION, HERBERT C. HAWTHORNE, VILA M. ROSENFELD, ANNA G. BUTLER, RUSSELL E. DAVENPORT, CHARLIE L. HARDEE, INEZ M. MYLES, B. F. NESBITT, KATHRYN G. KIRKPATRICK AND DAVID A. SMITH,

*Respondents.*

## REPLY BRIEF OF PETITIONER FLAV-O-RICH, INC. IN SUPPORT OF ITS PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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## REPLY BRIEF OF PETITIONER FLAV-O-RICH, INC. IN SUPPORT OF ITS PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

This case is before the Court on the Petition of Flav-O-Rich, Inc. ["FOR"], requesting that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fourth Circuit entered in this case on April 12, 1984.

In this Reply Brief FOR addresses the claims—advanced by Respondents, the North Carolina Milk Commission and its individual members, ["Respondents"], in their brief opposing grant of the writ sought by FOR—that the conduct contested by FOR in this action is exempt from antitrust scrutiny under this Court's decisions in *Parker* v. *Brown*, 317 U.S. 341 (1943), ["*Parker*"], and *California Retail Liquor Dealers Association* v. *MidCal Aluminum, Inc.*, 445 U.S. 97 (1980), ["*MidCal*"].

## I. THE FOURTH CIRCUIT HAS FAILED TO APPLY PROPERLY THE RULES ENUNCIATED BY THIS COURT IN *PARKER* AND *MIDCAL*.

In response to FOR's Petition to review the lower courts' application of the rules of *Parker* and *MidCal*, Respondents first argue, as they did in both the district court and the court of appeals, that their ". . . action in enforcing the state's statute prohibiting sales of milk below cost is the same as the state itself acting." Respondents' Br. at 8. This, they assert, ought to have ended the lower courts' inquiry. The closer analysis mandated by *MidCal* and by this Court's recent decision in *Hoover* v. *Ronwin*, ___ U.S. ___, 104 S.Ct. 1989, 80 L.Ed.2d 590 (1984), when the action challenged is *not* that of the state itself, but of others acting pursuant to state authorization, is not, they assert, required here.

The Respondents' argument ignores the factual finding—made by the district court and affirmed by the Fourth Circuit—that although Respondents are instrumentalities of the state, they are *not* the state itself. App. at 2a, 6a. By this argument Respondents tacitly invite this Court to ignore Rule 52(a) of the Federal Rules of Civil Procedure. However, Respondents have made no showing that the finding they dispute is clearly erroneous. To deny review based upon an assertion which is at variance with the factual findings of the lower courts, without first determining that those findings are clearly erroneous, would be—we respectfully submit—manifestly unfair to both FOR and the lower courts.

That preliminary matter aside, FOR will now discuss the arguments raised by the Respondents as they relate to the legal errors in the Fourth Circuit's application of *Parker* and *MidCal*.

### A. Respondents' Unauthorized Dissemination Of Milk Price Data Is Not Entitled To Antitrust Immunity Under *Parker*.

This is not a case which involves the authority of the State of North Carolina to proscribe below cost or predatory pricing of

fluid milk and dairy products as claimed by the Respondents. What is at issue is the anticompetitive and prohibited dissemination by the Respondents of highly sensitive and confidential price data as part of a scheme to set minimum wholesale milk prices in an unauthorized fashion.

The record established in the district court clearly demonstrates the unauthorized manner in which the Respondents have eliminated competition. At a January 13, 1976 Commission meeting, four possible approaches for "stabilizing the industry" were considered:

1. "The most desirable approach for stabilizing the industry would be for the Commission to set prices and control rebates at all levels."
2. "A second approach . . . would be adopting or reinstating a fair trade practice order."
3. "The third suggestion to the committee was that *an investigation of below cost selling by processors might have some merit.* . . . the Asheville market had been suggested as a place to begin such an investigation. . . ."
4. "[A]nother suggestion was that the Commission might see fit to set . . . minimum floor price[s]. . . ."

The Commission considered each of these four ways of "stabilizing the industry" and thus established its true objective—the elimination of competition. Of the four methods proposed by the state's processors to "stabilize the industry" the Commission selected the third—the use of below cost investigations and the filing of price information in connection therewith.[1]

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[1] It is significant to note how the "problem," in which this action has its genesis, arose. Sometime prior to April, 1974, Arcadia Dairy Farms began to import milk powder from Wisconsin, mix it with water and milk solids and sell it as reconstituted milk in the Asheville, North Carolina area at prices less than the price of whole milk. Asheville area processors and producers complained to the Commission, and the Commission adopted a rule which required Arcadia to pay money into an "equalization fund" in order to force up the price of this milk. Arcadia brought an action to have the "equalization rule" declared unlawful, and the North Carolina Supreme Court agreed that

Since that time, the Commission has continued to stabilize wholesale prices in this same unauthorized and prohibited manner. North Carolina statutes clearly provide only for a different and direct method of setting wholesale milk prices if the Commission wishes to do so. This procedure requires notice, public hearings and input from representatives of the milk industry and consumer groups as well. N.C.G.S. §§ 106-266.8(9) and (10). However, the evidence of record demonstrates that the Commission has ignored the required procedures and has instead continued to implement the following procedure of stabilizing prices:

1. The Commission requires a processor to notify the Commission in writing before it makes a "below cost" sale to meet a competitor's price.

2. The Commission has advised all processors that they cannot reduce their prices to meet a competitor's price unless they advise the Commission of the name of the competitor and the competitor's price.

3. Once a processor complains about another processor's prices, the Commission staff investigates the complaint, and advises the complaining processor what price is being charged

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it indeed was unlawful. Appeal of Arcadia Dairy Farms, Inc., 289 N.C. 456, 223 S.E.2d 323 (1976).

Despite this rebuff from the North Carolina Supreme Court—the state itself—the Commission remained determined to see that prices increased and were stabilized. Seven days after the court handed down its decision in the *Arcadia* case, the Executive Secretary of the Commission reported to the Commission that "all companies operating in the Asheville market had filed cost data which indicated certain sales by some processors in the Asheville market were being made at prices which were below cost."

One month later, five processors (Biltmore, Sealtest, The Borden Company, FOR and Arcadia Dairy Farms) were cited for selling milk below cost in the Asheville market. Hearings were held on these citations. At those hearings, the Commission staff introduced evidence as to the wholesale prices charged by each of these dairies in a public hearing at which other processors were present. Subsequently, all five processors were found guilty and the Commission's decision *and the processors' prices* were published in a general circulation daily newspaper, the Raleigh News and Observer.

by the processor complained of so that the complaining processor can meet that price.

4. If it is determined that the processor complained of is selling "below cost," a citation is issued and a public hearing is held.

5. At the public hearing, the costs and prices of the complaining dairy are introduced into evidence and can be heard by anyone present.

6. Although the statute which the Commission purports to be enforcing only prohibits "below cost" sales when they are for the purpose of harassing or injuring a competitor and specifically permits a processor to sell milk "below cost" to meet the price of a competitor, the Commission Staff never attempts to determine if the processor complained of was, in fact, attempting to harass or injure a competitor of if he was meeting the prices of competitors.

7. The costs and prices of the processor complained of are attached to the minutes of the Commission's meetings and are given to all Commission members, including the members of the Commission who are in direct competition with such processor.

8. The hearings are often reported in the newspapers, and the processor's prices are sometimes stated.

9. Furthermore, and unrelated to specific "below cost" procedures, if particular prices are part of a "price war," the Commission staff attempts to persuade the processors involved to conspire to raise their prices on their own without resorting to "below cost" procedures.

The district court reviewed this evidence and determined, as a matter of fact, that public disclosure of price and cost data occurred in five separate ways. App. at 8a. The district court also found, as matters of both fact and law, that these disclosures operated to stabilize prices in violation of Section 1 of

the Sherman Act, 15 U.S.C. § 1. App. at 2a, 4a-5a, 9a. Respondents do not dispute this finding.[2]

Each of these five types of disclosure at issue are—we submit—unauthorized by law. As noted in FOR's Petition, these disclosures are unlawful for two reasons.

First, it is the public policy of the State of North Carolina articulated in both its antitrust and its milk laws to foster and preserve competition.[3] The milk law states:

> The sale of milk by any distributor or producer-distributor or retailer below cost for the purpose of injuring, harassing or destroying competition is hereby prohibited; and the offering for sale of milk by a retailer at below-cost prices to induce the public to patronize his store, or what is commonly known in the trade as using milk as a 'loss leader' is also hereby prohibited. However, milk may be sold below cost to meet competition if notice has been sent to the Commission by registered or certified mail identifying the competitor or competitors. At any hearing or trial

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[2] One of the methods used by the Commission has been found by the district court to be unrelated to the Commission's below cost authority. App. at 9a. This particular method of calling processors together at the Commission offices to blatantly discuss the stabilization of prices in "problem" areas, leading to informal agreements sanctioned and in fact sponsored by the Commission to set prices, is particularly egregious and lacks any protection from the cloak of legitimacy the Respondents have tried in their brief to create from their "below cost" authority.

[3] The authority of the State of North Carolina to enforce its prohibition against predatory or below cost pricing is not at issue here. Indeed, were the practice not specifically proscribed by the milk law it would nonetheless be prohibited by the state's antitrust law. N.C.G.S. § 75-5(b)(5) declares that whoever shall:

> . . . willfully destroy or injure, or undertake to destroy or injure, the business of any competitor . . . with the purpose of attempting to fix the price of any goods when the competition is removed

shall be guilty of a violation of law. State v. Atlantic Coal & Ice Co., 210 N.C. 742, 188 S.E. 412 (1936); Rose v. Vulcan Materials Co., 282 N.C. 643, 194 S.E.2d 521 (1973). What petitioner opposes, and what this suit is about, is the unauthorized disclosure of price and cost data assembled by the Respondents in the discharge of their statutory responsibilities.

> on a complaint under this section, evidence of sale of milk by a distributor or subdistributor or retailer below cost shall constitute prima facie evidence of the violation or violations alleged, and the burden of rebutting the prima facie case thus made, by showing that the same was justified in that it was not, in fact, made below cost or that it was not for the purpose of injuring, harassing or destroying competition, or that it was sold below cost to meet competition after notice has been sent to the Commission.N.C.G.S. § 106-266.19.

The district court found, as a matter of fact, that the disclosures effectuated by way of the procedures described above violated the antitrust laws. App. at 2a, 4a-5a, 9a. Because they do, they offend the policy of the State of North Carolina reflected in N.C.G.S. § 106-266.19 to foster and preserve competition.

Second, such disclosure of price and cost data, especially that dissemination unrelated to the Commission's below cost authority, violates both N.C.G.S. § 106-266.8(12) (which requires that only general compilations of pricing and cost information for any marketing area be made public) and § 106-258 (which requires that the plant records of processors regulated by the State Department of Agriculture, such as FOR be treated confidentially) which *specifically* prohibit public dissemination of price and cost data collected by the Commission.

Because the disclosures which give rise to this case are both undeniably anticompetitive and so clearly forbidden by state antitrust policy and by explicit statutory direction, they are not entitled to antitrust immunity under *Parker*. 317 U.S. at 351-52.

### B. Respondents' Activities Do Not Satisfy Either Portion Of The Tests For Antitrust Immunity Articulated By This Court In *MidCal*.

In its recent decision in *Hoover* v. *Ronwin*, *supra*, this Court explained that where, as here, the activity challenged as violative of the antitrust laws is that of a state agency or in-

strumentality rather than that of the state itself, closer scrutiny is required. *Id.*, 80 L.Ed.2d at 599-600. That closer analysis must be conducted, this Court held, by use of the two pronged test of *MidCal*. *Id.*

As we have demonstrated above, the actions challenged in this case—the dissemination of milk price and cost data and the unauthorized stabilization of milk prices—offend the policy of the state to foster and preserve competition as articulated in both the milk and antitrust laws *and* the express statutory command that such information be treated in a confidential manner.

Because the public dissemination of what should be confidential information so offends state law, it is not undertaken pursuant to a "clearly articulated and affirmatively expressed" policy of the state. *MidCal*, *supra*, 445 U.S. at 105. Indeed, as demonstrated in Section I of FOR's Petition and in Section I, A of this Reply Brief, the challenged activity is, if anything, proscribed by North Carolina policy and law.

The second prong of the *MidCal* test is the requirement that the activity of a state instrumentality or agency be subject to the "active supervision" of the state itself. *MidCal*, *supra*, 445 U.S. at 105-06; *Hoover* v. *Ronwin*, *supra*, 80 L.Ed.2d at 599-600. Respondents argue that North Carolina exercised the requisite degree of supervision because the Commission is, by virtue of the political process of appointment, subject to the control of the state. This argument misses the mark.

If all that is required to meet the "active supervision" requirement is appointment by the state, the second prong of *MidCal* would be rendered meaningless. This is particularly true where, as here, those appointed by the state have—in their zeal to arguably meet one part of their responsibilities—trample other specifically imposed restrictions on that conduct.[4] Were Respondents indeed actively supervised by the

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[4] In this regard the *Appeal of Arcadia Dairy Farms, Inc.*, *supra*, litigation is instructive. There the North Carolina Supreme Court had to intervene to curb the Respondents' attempt to overreach their statutory authority.

state they would have been unable to make the continuing series of disclosures complained of by FOR, some related to below cost procedure and some not, because such disclosures are expressly forbidden by the state itself. Thus, Respondents' arguments in its brief, that all the disclosures are specifically related to the Commission's pro-competition below cost authority and are thus protected, wholly misses the mark and FOR's petition should be granted.

## II. THERE ARE CONFLICTS BETWEEN THE FOURTH AND NINTH CIRCUIT WITH RESPECT TO BOTH *MIDCAL* PRONGS.

In its petition, FOR asserted, *inter alia*, that the Fourth Circuit's decision in this case conflicts with the Ninth Circuit's decisions in *United States* v. *Title Insurance Rating Bureau of Arizona, Inc.*, 700 F.2d 1247 (9th Cir. 1983), *["Title Insurance"]* and *Miller* v. *Oregon Liquor Control Commission*, 688 F.2d 1222 (1982), ["Oregon Liquor"]. Respondents dispute this claim arguing that the facts of each of these cases are so different that no conflict exists. Respondents' Br. at 21-24. We demonstrate here that it is the distinctions Respondents' suggest—and not the conflicts—which do not exist.

### A. North Carolina, Like Arizona, Has A Statutorily Evidenced Interest In Actual Competition.

Respondents claim that the Ninth Circuit's decision in *Title Insurance* is distinguishable from the Fourth Circuit's opinion in this case because the regulatory scheme at issue there was established by a statute which did not clearly articulate and affirmatively express state policy "to restrict competition." *Title Insurance, supra*, 700 F.2d at 1253; Respondents' Br. at 22-23. The Ninth Circuit determined that the Arizona legislature was evidencing "neutrality" with respect to the competing goals of unfettered competition and "the stability and growth of title insurance." *Title Insurance, supra*, 700 F.2d at 1253. Such neutrality, the Ninth Circuit concluded, failed to satisfy the first prong of *MidCal. Id.* Even Respondents do not dispute this result. Respondents' Br. at 22-23.

The regulatory scheme at issue in this action is, if anything, reflective of a procompetitive disposition by the North Carolina legislature. As discussed *supra* at 6-7, the North Carolina legislature has manifested a desire that there be *fair* competition in the sale of fluid milk and dairy products in North Carolina in N.C.G.S. § 106-266.19. It is thus evident that North Carolina has no clearly articulated policy—dictated by the legislature—to restrict competition. Indeed, if it has any policy at all it is simply to eliminate predatory pricing and to permit otherwise free and open competition.

Because the North Carolina milk law—like the Arizona title insurance law—does not manifest a clear and unmistakable legislative intent to restrict competition, the Fourth Circuit's decision in this case is different from the Ninth Circuit's in *Title Insurance* only in its result. Thus, there is a clear conflict between the Fourth and Ninth Circuits with respect to the first prong of the *MidCal* test.

### B. Like Oregon, North Carolina Does Not Sufficiently Supervise The Regulatory Scheme At Issue.

Respondents assert that the Forth Circuit's decision in this case does not conflict with the Ninth Circuit's decision in *Oregon Liquor* because there the court correctly determined that there was an inadequate measure of state supervision.

In *Oregon Liquor* the determination that state supervision was inadequate was premised upon the Ninth Circuit's factual finding that the Oregon Commission neither "establishes prices nor reviews the reasonableness of prices." *Oregon Liquor, supra*, 688 F.2d at 1226. However, the court also found that Oregon was empowered to and did "effectuate the price posting and the prohibition on quantity discounts and transportation allowances." *Id.* at 1227.

The statutory scheme adopted by the North Carolina legislature admittedly does more than the Oregon scheme. However, it does not " 'displace unfettered business freedom' with its own power." *Id. citing MidCal, supra*, 445 U.S. at 106 n. 9 *quoting New Motor Vehicle Board* v. *Orrin W. Fox Co.*, 439

U.S. 96, 109 (1978). Because it does not, a conflict clearly exists between the Fourth and Ninth Circuits with respect to the second prong of the MidCal test. The arguments raised by Respondents in their brief are without merit.

## III. CONCLUSION

For all the reasons set forth in its Petition and in this Reply Brief, FOR respectfully submits that its Petition For A Writ Of Certiorari to the United States Court of Appeals for the Fourth Circuit should be granted.

Respectfully submitted,

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September 17, 1984

## CERTIFICATE OF SERVICE

I hereby certify that on this 17th day of September, 1984, three copies of this Reply Brief were mailed, postage prepaid, to counsel for the Respondents, W.C. Harris, Esq. and F. Stephen Glass, Esq., Harris, Cheshire, Leager & Southern, P. O. Box 2417, Raleigh, North Carolina 27602.

I further certify that all parties required to be served have been served.

---

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